Before the
Federal Communications Commission
Washington, D.C.

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	

COMMENTS

The National Exchange Carrier Association, Inc. (NECA) submits these comments in the matter captioned above.[1] The Commission seeks comment on the Recommended Decision[2] of the Federal-State Joint Board on Universal Service (Joint Board) regarding a plan for reforming the rural universal service support mechanism, recommended by the Rural Task Force (RTF).[3]

I. BACKGROUND

On December 22, 2000 the Joint Board released its Recommended Decision, sending to the Commission the RTF proposal for reforming the rural high-cost mechanism. The Joint Board earlier had sought comment on the RTF Recommendation.[4]

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[1] *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Further Notice of Proposed Rulemaking, FCC 01-8 (rel. Jan. 12, 2001) (FNPRM).

[2] *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, FCC 00J-4 (rel. Dec. 22, 2000) (Recommended Decision). The Recommended Decision incorporates the Rural Task Force (RTF) Recommendation and offers it "as a good foundation for implementing a rural universal service plan that benefits consumers and provides a stable environment for rural carriers to invest in rural America." FNPRM, at para. 1, citing Recommended Decision at paras. 1, 10-13.

[3] *Id.* at para. 1.

[4] *Federal-State Joint Board on Universal Service Seeks Comment on Rural Task Force Recommendation*, Federal Communications Commission Public Notice, CC Docket No. 96-45, FCC 00J-3 (rel. Oct. 4, 2000).

In that proceeding, NECA filed comments supporting the RTF Recommendation, noting the need to consider the long term effects of any high cost fund capping mechanism, and commending the RTF for its work in developing a workable high cost plan for rural carriers, by achieving consensus among diverse industry interests.[5]

Among the key points of the RTF proposal were that the FCC Non-rural Synthesis Model, currently used to determine forward-looking costs for Non-rural carriers, should not be used for Rural carriers. The RTF proposed, instead, that the Commission adopt a modified version of the current universal service mechanism for rural areas. Also, the RTF proposal included suggestions for methods to develop disaggregated per-line support levels in Rural carriers' serving territories; a proposal that the Joint Board and the Commission adopt a "no-barriers to advanced services" policy; and a set of principles that the RTF believes should be used to address implicit support in interstate access charges, including development of a "High Cost Fund III" to take the place of any implicit support amounts removed from interstate access charges.[6]

Perhaps most notably, the RTF recognizes the need for some form of relief from the existing limitations on high cost support:

> The Rural Task Force's proposed modifications to the high-cost loop support mechanism include various upward adjustments to current limits on universal service support for rural carriers, including (a) recomputing the indexed cap on high-cost loop support and the corporate operations expense limitation . . ., (b) providing above-the-cap "safety net additive" support for carriers with over 14 percent

[5] National Exchange Carrier Association, Inc., Comments, *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Rural Task Force Recommendation, FCC No. 00J-3 (fil. Nov. 3, 2000) (NECA Comments).

[6] Recommendation at 4.

> growth in telecommunications plant in service on a per-line basis, and (c) creating a "safety valve" to provide additional support for "meaningful investment" in acquired telephone exchanges. . . Under the Rural Task Force's proposal . . . [these support components] would be excluded from the cap on high cost loop support. Total "safety valve" support would be limited to five percent of the overall cap.[7]

The proposals set forth by the RTF demonstrate remarkable compromises among industry segments that traditionally have not found common ground. Yet, the proposals are reasonable, and, in NECA's view, workable. Because the RTF proposals were forged in a "crucible of compromise," they convey integrity of purpose, and strengths drawn from the RTF members' shared vision. The Commission, therefore, must give the Joint Board Recommendation on the RTF proposals extraordinary weight as it considers reforming universal service for the long term.

II. DISCUSSION

A) NECA Agrees That The Non-rural Synthesis Model Methods Will Not Work For Rural Carriers.

NECA's Comments observed that the RTF had conducted extensive analysis of the FCC Non-rural Synthesis Model as a potential tool for developing support for Rural carriers.[8] RTF concluded from these analyses that the model is an inappropriate tool for establishing forward-looking costs of Rural carriers, stating that "when viewed on an individual rural wire center or individual Rural Carrier basis, the costs generated by the

[7] RTF Recommendation at 1-5, 6 (notes omitted).

[8] NECA Comments at 2, citing RTF Recommendation at 17-18.

Non-rural Synthesis Model are likely to vary widely from reasonable estimates of forward-looking costs."[9]

The RTF's results are consistent with NECA's own analyses, which show that the Non-rural Synthesis Model methods produce greatly distorted results for Rural carriers, whose serving areas, customer bases, and operating characteristics vary greatly, not only from those of Non-rural carriers, but among Rural carriers themselves.[10] RTF went on to note that using the Non-rural Synthesis Model to size a national rural high cost fund would reduce available support for Rural carriers by more than one billion dollars, to $451 million.[11] The RTF identifies as the reason for this drastic reduction the FCC decision to use a nationwide benchmark and statewide cost-averaging for determining a 'sufficient' level of federal funding for Non-rural carriers.[12] RTF describes the effect of this methodology:

> Because Rural Carriers represent only a fraction of the overall industry, their addition in determining the national average cost benchmark changes the average by only a small amount, even though as a group the average total cost of service for Rural Carriers is more than twice that of Non-rural Carriers. For the same reason, averaging the cost of Rural Carriers with the costs of all other carriers within a state would eliminate funding for many Rural Carriers. Thirty-seven states, territories, and protectorates which receive federal universal service support for Rural Carriers today would receive zero support if statewide cost-

[9] RTF Recommendation at 18.

[10] *See* NECA *Further Comments on Cost Models*, Federal-State Joint Board on Universal Service, CC Docket No. 96-45 (filed Aug. 9, 1996).

[11] RTF Recommendation at 19.

[12] *Id.*

> averaging and a national benchmark were used in sizing the universal service fund available to Rural Carriers.[13]

NECA agrees that, as the RTF analysis shows, such an approach would have adverse impacts on universal service in areas served by Rural carriers. Reductions in interstate universal service funding caused by this methodological change would exert upward pressure on state funding mechanisms and cause local rates to rise to levels unaffordable for many, results that are at odds with the Commission's universal service policies.

B. The Commission Should Adopt The Recommendation For Continued Use of the Current Embedded Cost Mechanism with Modifications.

The Recommendation suggests continued use of the existing embedded cost mechanism to determine high cost loop (HCL) universal service funding for Rural carriers, with certain modifications. Specifically, the RTF recommended that the HCL fund should be "re-based" by increasing it $118.5 million, then grown by an annual factor. The RTF also recommended that the current limitation on corporate operations expenses be adjusted for growth, and that a "safety valve mechanism" be added to the current limitation on support for acquired or transferred exchanges.[14]

The RTF's recommendation to revise the indexed cap on universal service is a material improvement over current rules.[15] When the cap was initially implemented, its

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[13] *Id.* (notes omitted).

[14] *Id.*

[15] RTF's proposal to re-base the high cost fund would return approximately $118.5 million annually to the fund, including $83.9 million for the indexed fund cap and $34.6 million for the corporate operations expense limitation, based on October 1, 1999 data and calculations supplied by NECA to RTF. *Recommendation,* at note 46.

effects on universal service funding were relatively minor. In 1994, for example, payment shortfalls associated with the cap amounted to about $36 million, or less than 4% of the high cost fund requirements. In the year 2001, seven years after the "interim" cap was imposed, payment shortfalls are expected to total nearly $198 million, almost 18% of total fund payments. In all, payment shortfalls caused by the interim cap since 1994 have totaled over $483 million, including nearly $133 million in year 2000 payments.[16] These continuing shortfalls are inconsistent with the requirements of the Telecommunications Act for "specific, predictable and sufficient" universal service funding.

The RTF's proposal to re-base the overall cap on the HCL fund represents a major step forward, and is all the more noteworthy because it represents a consensus decision reached among various industry groups over the course of the past two years. Any capping mechanism, however, carries the risk that universal service funding will again deteriorate in the future, particularly as Rural carriers seek to deploy facilities with advanced service capability. NECA recommends that the Commission take account of this risk as it considers this part of the RTF's Recommendation.[17]

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[16] Federal-State Joint Board on Universal Service: *Promoting Deployment and Subscribership in Unserved and Underserved Areas, Including Tribal and Insular Areas*, CC Docket No. 96-45, *Further Notice of Proposed Rulemaking*, 14 FCC Rcd. 21177 (1999), Joint Comments of NECA and USTA (Dec. 17, 1999).

[17] For example, an integral component of the recently-filed Multi-Association Group (MAG) Petition for Rulemaking is an amendment to the Commission's Part 36 rules, which would eliminate the indexed cap on the high cost fund. (The Commission recently issued a Notice of Proposed Rulemaking on the MAG Petition.) *See In the Matter of Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return*

The Recommendation also would allow an adjustment for growth in the corporate operations expense limitation that is included in the loop cost calculation that determines high cost support "expense adjustment" amounts.[18] RTF would "re-base" and index the amounts included in the loop cost calculation, and would add an alternative methodology for determining the assignment of corporate operations expense.[19] NECA supports this proposal, as part of a "next-best" alternative to removing the limits on high cost support mechanisms entirely, *e.g.,* as proposed in the MAG plan (see n.17, *supra*). In particular, the alternative proposed by RTF will relieve many small Rural carriers of the burden and expense of going through the waiver process, if corporate operations expenses exceed the limits of section 36.621(a)(4) of the Commission's rules.[20]

NECA also agrees with RTF that the problems created by section 54.305 of the Commission's rules should be addressed by the Joint Board and the Commission.[21] As the Recommendation states, customers in high cost rural exchanges must not be "doomed" to poor service because they live in exchanges that have been involved in sale

Regulation, CC Docket No. 98-77, *Prescribing the Authorized Rate of Return For Interstate Services of Local Exchange Carriers*, CC Docket No 98-166, Notice of Proposed Rulemaking, FCC 00-448 (rel. Jan. 5, 2001) at Appendix A, Exhibit 3, proposed amendment to 47 C.F.R. § 36.601(c), p.3 - 2 (MAG Petition).

[18] Recommendation, at 27 - 28.

[19] *Id.* at 28.

[20] 47 C.F.R. § 36.621(a)(4).

[21] *Id.*, at 29. Section 54.305 limits high cost payments for transferred exchanges to the level of the transferring carrier.

or transfer transactions.[22] According to the Recommendation, "in many cases, this Section limits the ability and motivation of the acquiring entity to make new investments to upgrade the networks in these acquired properties in spite of their high cost and rural nature."[23] In addition, it places a very complex and significant administrative burden on small companies by effectively requiring them to maintain two sets of accounting records to distinguish costs associated with "acquired lines" from costs associated with "previously owned" lines.

As a specific solution to this problem, the RTF proposal includes provision of a safety valve mechanism, "to enable rural carriers acquiring access lines eligible for high-cost loop support to recover additional support reflecting 'meaningful investment' in acquired access lines."[24] The Joint Board supports the proposal for "additional support to rural carriers . . . acquir(ing) high-cost exchanges and mak(ing) post-transaction investments" that improve the network.[25] But the Joint Board urges the Commission to consider several implementation issues which it (the Joint Board) believes are not

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[22] *Id.* NECA and the national telephone associations previously have stated in this docket that section 54.305 of the Commission's rules acts as a disincentive to carriers to upgrade loop plant in such cases, that the rule impedes modernization, and that it slows deployment of advanced services in rural America. NECA and other parties advocated, therefore, that the rule should be eliminated. *See* Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Recommended Decision*, Comments of NECA, NRTA and OPASTCO (filing jointly) (Aug. 14, 2000). *See also* the MAG Petition (ref. n. 17, above).

[23] Recommendation, at 29.

[24] FNPRM at 16, citing Recommendation at A-29.

[25] *Id.* at para. 16

addressed by the RTF proposal.[26] Thus, the Commission seeks comment on: 1) distribution of safety valve support when the total amount of eligible support exceeds the cap of five percent of the indexed high cost fund; 2) the definition of "meaningful investment"; 3) whether safety valve support is transferable in exchange transfers; and 4) whether safety valve support is frozen when a competitive carrier enters the study area, and whether such an approach might unduly deter investment.[27]

The limitation on high cost support imposed by section 54.305 on exchange sale transactions adds unnecessary complexity to the process and acts as a deterrent to improving universal service in rural areas. It should therefore be eliminated entirely. As the Joint Board's questions reveal, the addition of a "safety valve" mechanism to the current rule is likely to complicate the process even further. Nevertheless, as a "next-best" alternative to eliminating the rule, the Commission should consider implementing the RTF recommendation in this regard.

In the interests of fairness, rules governing distribution of "capped" safety valve support in cases where the cap is exceeded should permit *pro rata* adjustment of shortfalls among all carriers receiving such support. This would be preferable to a "first-come, first-served" approach, which might force carriers to complete acquisition sooner than anticipated, while providing no assurance that funds eventually would be available.

The Commission should not attempt to impose any special definitional qualifications on the type of investments qualifying for safety valve support. Current Part 32 accounting rules and Part 36 USF expense adjustment rules have served the

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[26] *Id.* at para. 17.

[27] *Id.*

Commission well in identifying the types and amount of costs eligible for high cost support; additional definitions are unnecessary. Similarly, NECA does not believe it necessary to develop special rules governing treatment of safety valve support in cases where exchanges are subsequently transferred, or where competitive entry occurs. Rather, these support amounts should be treated in the same manner as basic support amounts associated with particular high cost areas.

NECA also supports the RTF proposal for a "safety net" additive to supplement fifty percent of the difference between the capped "expense adjustment" for the study area and the uncapped amount for the study area.[28] Again, as a next-best alternative to removal of the high cost fund cap, this proposal should be given serious consideration by the Commission, if the cap is not removed totally.

NECA also concurs with RTF's observations about potential difficulties associated with the time lag between provision of service and receipt of universal service funding. The Recommendation states, and NECA agrees, that this lag should be as short as technically and administratively feasible.[29] The phenomenon RTF identifies not only contributes to distortions in distribution of support between incumbent carriers and new entrants, but has serious adverse impacts on carriers seeking to serve new territory, for which prior-year operating results may not be available on a timely basis. NECA encourages the Commission to seriously consider RTF's recommendation for a loop-counting formula that would more accurately represent the reporting period, as well as shorten the lag between service provision and payments.

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[28] RTF Proposal at A-27.

[29] *Id.* at 38.

I. CONCLUSION

The Joint Board has strongly endorsed the RTF Recommendation. NECA agrees with the RTF that, if adopted, its proposals will help assure sustained and adequate universal service for rural areas. The RTF properly recognizes, as does the Joint Board, that carriers serving rural high-cost areas are different from Non-rural carriers, that a separate high-cost fund mechanism must be maintained for Rural carriers, and that other badly-needed reforms in the universal service rules must be adopted quickly. The Joint Board Recommendation should be adopted immediately by the Commission, with due consideration of the potential longer-term effects of imposing artificial limits, such as continuation of any form of capping, on the size of the Rural carrier high cost fund.

Respectfully submitted,

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